

## **Testimony to the Special Joint Committee on Initiative Petitions**

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Jim Stergios, Pioneer Institute

Good morning. My name is Jim Stergios, and I serve as executive director of Pioneer Institute. Thank you for the opportunity to testify in support of a gradual personal income tax reduction, spread in 3 tranches over 3 years and an adjustment to the revenue growth limit statute.

I believe the ballot questions that we will discuss today are actions the legislature should itself take. Here's why.

Massachusetts is at a competitive and affordability turning point. We face a choice.

### **The Urgency**

The Commonwealth is losing its most precious asset—talent — as well as business investment, and economic dynamism. Out-migration has worsened sixfold in just the past 15 years, and those who are leaving are disproportionately young workers and families.

When they leave, they take with them entrepreneurship, investment, and future tax revenue, and they strip us of our long-term strength. We see this in the data on business formation. For 20 years, Massachusetts was a strong national performer on business formation, and we led New England by far in entrepreneurship. Now we both trail New England and the nation.

In recent years, 26 states have chosen to reduce taxes—reining in the spikes in spending that began with a COVID emergency. We have not. They have cut taxes and reined in spending, and they have outcompeted us for our residents, our employers, and our investment.

North Carolina is a particularly instructive example. North Carolina — and, in particular, the Research Triangle and Charlotte — is a very good proxy for Massachusetts, with a similar industry mix, including finance, medical innovation, STEM, and higher education. It is a purple state.

Since 2014, North Carolina has steadily lowered its flat personal income tax from 5.8% to 4.25%. It will soon be under four percent. It has also lowered its corporate tax from 6% to 2.25%, which it will, in fact, eliminate in 2030.

It has, since 2020, increased its job base by 450,000 jobs, or by 12%. Massachusetts, over the same time, has lost 20,000 private sector jobs—one of just three states to lose jobs. North Carolina is far outpacing Massachusetts on STEM jobs—a sector we have built our economic reputation and strength on.

### **The Opportunity**

Had Massachusetts matched North Carolina's rate of growth, it would have added 377,000 jobs since 2020.

That's not an abstract number. That's livelihoods and attracting and keeping the young. But for state budgets, it is also a source of \$2 billion a year in state revenue through income, sales, and other tax collections. Competitiveness creates jobs, it keeps people in Massachusetts, and it broadens the tax base. It strengthens the state fiscal position.

One reason Massachusetts is underperforming, compared to other states, is that the state tax structure is particularly punitive to our homegrown small and midsize businesses that are most likely to expand and hire. 140,000 of our 756,000 businesses are organized as pass-through entities—for example, LLCs. Their business income is taxed through the personal income tax. That income most often is reinvested in payroll, equipment, and inventory—in expansion and jobs.

These firms are not peripheral to Massachusetts job seekers. Pass-through businesses employ 1.5 million workers in the Bay State, and the proposed cumulative one percent cut amounts to a 20% tax cut for the small business community. That's why this tax proposal would create 43,000 to 48,000 jobs.

### **The Proposed Reduction in the Personal Income Tax**

Yes, we have heard the sky-is-falling numbers from insiders and critics. That is just scaremongering. Why? Consider these two points.

Over the last 15 years, the growth in state spending has doubled the rate of growth of median household income. That is not a sustainable path—the state is lapping the taxable capacity of its residents.

Second, history shows modest tax cuts, implemented gradually, are manageable.

In 1999, Massachusetts had a 5.95% personal income tax rate which raised \$8 billion. In FY 2000, the legislature lowered that rate to 5.85%, and revenues went up \$1 billion. In FY 2001, the rate was further lowered, because of a ballot initiative, to 5.6%, and revenues went up another \$900 million. That's over 24 percent revenue growth in just two years.

In 2002, the tax rate was lowered to 5.3%, and there was a decline that year, largely due to the dot-com bust and 9/11. Approximately \$530 million in revenues were lost directly related to the cut in the personal income tax.

In 2003, tax revenues already stabilized, growing by \$100 million, and thereafter grew through 2008. From 1999, before the first tax cut, to 2008, personal income tax revenues grew from \$8 billion to \$12.5 billion, a 56 percent increase.

After the Great Recession, the state implemented six incremental (0.05%) reductions to arrive at the statutory 5.0% rate. Revenues grew over that time in real, inflation-adjusted terms as well.

Critics—as can be seen from the *2000 Voter Handbook*—were claiming a \$2.7 billion to \$3 billion hit to state tax revenues. The empirical record does not support that kind of alarmism and scaremongering.

That's the history. In a moment, Rebekah Paxton, a Boston University-trained economist who previously worked at Pioneer and now works on a broad set of national economic issues, has built a dynamic (rather than a static) model that suggests a path similar to what we saw in 2000.

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Massachusetts residents and businesses are hurting now, feeling the result of inflation and state policies that have driven up the cost of housing, healthcare, and energy. The income tax cut provides immediate help with affordability—which is a crucial reason people are leaving the state.

It provides immediate incentives for small and mid-sized businesses to invest—something Mass Opportunity Alliance polling shows they are ready to do. The gradual reduction we propose will lead to the creation of 43,000 to 48,000 new jobs. That is tens of thousands of people working, earning income, supporting families, paying taxes, and contributing to the Commonwealth's civic and economic life.

You have before you today a choice. I would urge the legislature itself to implement this broad-based rate reduction. It's a path that requires short-term fiscal discipline by the state but immediately puts money in people's pockets, creates almost 50,000 jobs, increases patents and GDP. It's a choice that, in a short span of years, will have the state collecting, in real, inflation-adjusted terms, more tax revenue than it is today.

### **The Revenue Cap Proposal**

A few remarks on the history of the state's revenue growth limit and the ballot proposal to update the formula the state uses to implement it.

The revenue growth limit was established in law as Chapter 62F after being passed by the voters in 1986—and, since that year, it has been triggered only twice—once in 1987 and more recently in 2022.

Many people, including those in government, had forgotten about the revenue growth limit statute, until four years ago when it triggered the return of \$3 billion in excess revenue to the taxpayers.

It was forgotten because the formula applied by the Legislature veered away from the law's original intent. The original law was adopted by referendum because the people wanted a straightforward, common-sense taxpayer protection: They wanted to limit the growth of state tax revenues to the growth in taxpayer earnings.

Something that people in the building forgot. Again, Rebekah Paxton will speak to the economics of the proposed change we seek. Our goal is simple: To have the law do what it was intended to do.

### **Conclusion**

As I stated at the start, as state leaders, you have a choice. You can stay the course and manage the decline of the great Massachusetts economy—leaving it an economy with weak business

formation, lagging job growth, higher unemployment, high costs, continued out-migration, and ultimately fewer taxpayers paying higher taxes.

Or you can choose to advance these two proposals. They are measured and advance gradual shifts in taxation and revenue management that will improve affordability, the business climate, job creation, and the retention of younger workers and families. That's a stronger Commonwealth.

The proposals are not radical; they are gradual. And history suggests the near-term impact on the state budget will be far more modest than opponents claim today.

I'm deeply grateful for the opportunity to testify.